SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 338

FRANK A. BERRY AND MILLER WALTON,
Petitioners,
vs.

C. J. ROOT, FIDUCIARY COUNSEL, INC., AUGUSTUS T. ASHTON, E. B. CONNOLLY, PARKER MAXWELL, AND THE UNKNOWN HOLDERS OF $42,000 PAR VALUE OF BONDS SOUGHT TO BE AFFECTED BY THE SO-CALLED PLAN OF COMPOSITION

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

I

The Opinion of the Court Below

The opinion of the Circuit Court of Appeals for the Fifth Circuit was rendered April 25, 1945 (11174, pp. 63-68), and is reported as *Berry* v. *Root,* 5 Cir., 148 F. 2d 945. A petition for rehearing (11174, pp. 69-79) was denied May 17, 1945 (11174, p. 80).

II

Statement of Jurisdiction

A statement of the grounds on which the jurisdiction of this Court is invoked is contained in the foregoing

Petition (pp. 7-9), and in the interest of brevity, is adopted as a part of this Brief.

III

Statement of the Case

A statement of the case is contained in the foregoing Petition (pp. 1-7), and in the interest of brevity, is adopted as a part of this Brief.

IV

Specification of Errors

The Court of Appeals erred in the following respects:

1. In affirming the orders of the District Court.

2. In deciding that the District Court lacks jurisdiction to make the allowance sought.

3. By misconceiving the "true question" presented.

4. By denying the existence of an historic equity power of courts of bankruptcy.

5. In deciding that it was not permissible for petitioners to seek the allowance directly to themselves.

V

Argument in Support of Petition

Point I

The decision of the Court of Appeals is in direct conflict with controlling principles enunciated by this Court in *Trustees* v. *Greenough,* 105 U. S. 527; *Randolph* v. *Scruggs,* 109 U. S. 533; *Sprague* v. *Ticonic Natl. Bank,* 307 U. S. 161; *Securities & Exchange Comm.* v. *United States R. & I. Co.,* 310 U. S. 434; *American United Mut. L. Ins. Co.* v.

Avon Park, 311 U. S. 143; *Reconstruction Finance Corp.* v. *J. G. Menihan Corp.*, 312 U. S. 81, and *Young* v. *Higbee Co.*, 324 U. S. 204.

The Court of Appeals reasoned: A court of bankruptcy "is not a court of equity," but is a statutory court created and governed by the Bankruptcy Act, and as to original bankruptcy proceedings, the Act "has not adopted the equity precedents and practices as to costs, including costs as between attorney and client, commonly called an allowance of attorney's fees" (11174, p. 65), Chapter IX of the Act "carefully defines the attorney's fees that may be allowed, to be provided for in the plan of composition," and no others can be allowed (11174, pp. 66).

This Court has decided: "Courts of bankruptcy are courts of equity and exercise all equitable powers unless prohibited by the Bankruptcy Act."[7] When exercising municipal composition jurisdiction, "A bankruptcy court is a court of equity, * * * and is guided by equitable doctrines and principles except in so far as they are inconsistent with the Act * * *;" and the many cases cited "indicate the range and type of the power which a court of bankruptcy may exercise in these proceedings. *That power is ample for the exigencies of varying situations. It is not dependent upon expressed statutory provisions. It inheres in the jurisdiction of a court of bankruptcy.*"[8] "Good sense and legal tradition alike enjoin that an Act of Congress dealing with bankruptcy should be read in harmony with the existing system of equity jurisprudence of which it is a part."[9] "It is also established by sufficient authority, that where one of many

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[7] *Young* v. *Higbee Co.*, 324 U. S. 204.

[8] *American United Life Ins. Co.* v. *Avon Park*, 311 U. S. 143—Emphasis supplied.

[9] *Securities & Exchange Comm.* v. *United States R. & I. Co.*, 310 U. S. 434.

parties having a common interest in a trust fund, at his own expense takes proper proceedings to save it from destruction and to restore it to the purposes of the trust, he is entitled to re-imbursement, either out of the fund itself, *or by proportional contribution from those who accept the benefit of his efforts.*"[10] That principle applies in bankruptcy proceedings, because a petition "to have a debtor adjudged bankrupt is for the benefit of all his unsecured creditors; and a favorable decree gives them all a proportionate advantage, and the court has no power to order * * * that this advantage shall depend upon their contributing to the expenses of the suit; but any creditor may carry on the proceedings * * *; and after adjudication all may prove their debts. * * * no single creditor nor any three or four of them have a sufficient interest to enable them to undertake the conduct of the proceedings without positive loss of money if they cannot tax the expenses on the fund, for those expenses will usually exceed the dividend on their debts."[11]

The principle applied in *Randolph* v. *Scruggs, supra,* decided under the Bankruptcy Act of 1898, is that a court of bankruptcy should follow the "equity precedents and practices" and allow, as equitable costs, attorneys' fees not expressly provided for by the Act.

Trustees v. *Greenough, supra, Sprague* v. *Ticonic Natl. Bank, supra,* and *Reconstruction Finance Corp.* v. *J. G. Menihan Corp., supra,* enunciated the principles that there are at least two classes of cases in which equitable costs "as between solicitor and client" are assessed: first, where a party wrongfully brings suit and is required to bear

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[10] *Trustees* v. *Greenough,* 105 U. S. 527—Emphasis supplied.

[11] *Trustees* v. *Greenough,* 105 U. S. 527, 534, quoting with approval the opinion of Judge Lowell in *In re Jaffray,* D. C. Mass., Fed. Cas. No. 7170, 13 Fed. Cas. 284, 2 N. B. R. 452.

the burden, although there is no fund in Court; second, where a party is the beneficiary of litigation and is required to bear his share of the burden, either from a fund in Court or "by proportional contribution" to those who conferred the benefits; but the source of the power is the same in both classes—the historic power and authority of a Court exercising jurisdiction "in equity" to do equity in a particular situation.[12]

The fundamental principle affirmed by the cited decisions is that once the statutory jurisdiction of a court of bankruptcy is invoked and attaches, the Court then has broad power and jurisdiction "in equity" to grant all forms of equitable relief, and is not impotent to do justice and equity among the parties to the proceeding.

Counsel urges that the questions presented are controlled by the foregoing principles, whose application to closely analogous facts is strongly emphasized by the recent decision in *Young* v. *Higbee Co., supra.* The factual situations are parallel, except that in the cited case the appealing stockholders abandoned their appeal and "sold out" the asserted rights of their class, but in the instant case the appealing creditors, by good faith prosecution of their appeals and defense of the certiorari proceeding,

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[12] "It is true that in many cases wherein costs have been allowed to the prevailing party as between solicitor and client rather than as between party and party, they were allowed, as in *Sprague* v. *Ticonic Bank, supra,* and in our case of *O'Hara* v. *Oakland County,* 136 Fed. (2d) 152, because a fund had been brought into court by reason of the proceeding, to the benefit of the plaintiff or to the members of a class. But it is clear from the *Sprague* case and other adjudications, that the doctrine is not limited to such situations but may be invoked against one of the parties as 'fair justice' to the other will permit, and that the allowance of such costs in appropriate situations is part of equity jurisdiction of which the federal courts were given cognizance ever since the first Judiciary Act consisting of that body of remedies, procedures, and practices which theretofore had been evolved in the English Courts of Chancery." *Cleveland* v. *Second Natl. B. & T. Co.,* 6 Cir., 149 F. 2d 466.

succeeded in conferring valuable benefits on their class. In each case, the objections to confirmation contained no formal class suit allegations, the appeals were in the names of only the appealing parties and did not specify that they were in the interest of the whole class, the appeals sought no individual relief but only to have the confirmation set aside, they were not from the denial of individual claims but were on the bases that every member of the class was injured by the confirmation, the controlling issues were such that the rights of the appealing and non-appealing members of the class were inseparable, the success or failure of the appeals was bound to have a substantial effect on the interests of all members of the class, and the primary object of the appeals was to add value to the claims of all members of the class.

The decision was that, by taking their appeal, the appealing stockholders had assumed temporary control of the common rights of all members of their class and were under a duty fairly to represent those common rights; and had they done so successfully, instead of selling out, they would have added value to the claims of all members of their class. For those reasons, it was decided that the appeal was, in reality and legal effect, taken in a representative capacity, on behalf of the entire class, and the appealing stockholders should be compelled to account to the other members of their class for the proceeds of the rights they had sold.

The Court pointed out that the representative responsibility of the appealing stockholders was emphasized by the fact that they "might have been awarded compensation for their services had they succeeded in reducing the claim of the junior indebtedness to the advantage of all the preferred stockholders."

Had Petitioner's clients violated their self-imposed trust by abandoning their appeals and "selling out" the asserted

rights of their class, the other members could have invoked the equity jurisdiction of the bankruptcy court to compel an accounting. Because rights in equity are reciprocal, the converse must be true. The trust having been faithfully executed by the successful and beneficial prosecution of the appeals, the bankruptcy court does not lack jurisdiction to grant equitable relief against those who received and accepted the benefits.

Point II

The decision sought to be reviewed is in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *In re Lacov*, 142 F. 960, the decision of the Circuit Court of Appeals for the Third Circuit in *In re Keystone Realty Co.*, 117 F. 2d 1003, the decision of the Circuit Court of Appeals for the Fourth Circuit in *Receivers* v. *Staake*, 133 F. 717, the decision of the Circuit Court of Appeals for the Seventh Circuit in *In re Swartz*, 130 F. 2d 229, and the decision of the Circuit Court of Appeals for the Eighth Circuit in *Summers* v. *Abbott*, 122 F. 36.

In *In re Lacov, supra*, the Court decided that a court of bankruptcy has jurisdiction, under its general equity powers, to order the petitioning creditors to pay the expense of a receivership, where the receiver was appointed on their application which was subsequently dismissed as unfounded. The court said: "There is no express provision in the bankruptcy act, which authorizes the court of bankruptcy to compel petitioning creditors to pay the costs of a receivership under such circumstances * * *."

In *In re Keystone Realty Co., supra*, the court construed § 258 of the Act, relating to costs in corporate reorganization proceedings, and held that, because a court of bankruptcy is a court of equity, the authority to tax costs should be construed in accordance with equity principles, consequently, that the court of bankruptcy was authorized to allow attorneys' fees as equitable costs "as between solici-

tor and client." The court cited *Trustees* v. *Greenough, supra,* and *Sprague* v. *Ticonic National Bank, supra.*

In *Receivers* v. *Staake, supra,* the Court decided that attaching creditors who seized, prior to bankruptcy, property which subsequently passed into the hands of trustees in bankruptcy, were entitled to be paid reasonable fees from a fund produced by a sale of property. This was on authority of *Trustees* v. *Greenough, supra.*

In *In re Swartz, supra,* the Court decided that after confirmation of a plan of composition under former § 74, the court of bankruptcy could tax equitable costs, including attorney fees, against creditors who filed groundless claims and prosecuted them in a manner that unwarrantedly interfered with and delayed the proceeding. The Court pointed out that a composition proceeding is a proceeding in equity, and that costs not otherwise governed by statute are given or withheld, in the sound discretion of the Court, acocrding to the facts and circumstances of the case; citing *Guardian Trust Co.* v. *Kansas City R. Co.,* 8 Cir., 28 F. 2d 233, and *Sprague* v. *Ticonic Natl. Bank, supra.*

In *Summers* v. *Abbott, supra,* the Court decided that an assignee for the benefit of creditors, on turning over the assets to a Trustee in bankruptcy, was entitled to compensation for his own services *and those of his attorneys.*

It also is noteworthy that in *Beach* v. *Macon Grocery Co.,* 125 F. 513, the Circuit Court of Appeals for the Fifth Circuit decided that all costs and "expenses" of a bankruptcy receivership should equitably be taxed against petitioning creditors who erroneously secured the appointment of the receiver. This was not an assessment of party to party costs, but of costs "as between Solicitor and client."

The decision sought to be reviewed obviously conflicts not only with the cited decisions from other Circuits, but also with the earlier decision by the same Court of Appeals.

Point III

The jurisdiction "in equity" and to assess, apportion and render judgments for "costs," conferred by §§ 2a and 2a(18) of the Act, empower a court of bankruptcy to award solicitors' fees as equitable costs "as between solicitor and client," in a municipal composition proceeding under Chapter IX of the Act, for successful appellate services that conferred material benefits on all members of an affected class of creditors.

The Court of Appeals reasoned: "The original Act and all its amendments and expansions have dealt specifically with the costs and attorney's and other fees to be allowed, and have dealt jealously with them. The fees allowable for services in each kind of bankruptcy proceeding have been provided, and expressly or by implication others are excluded" (11174, pp. 65-66). § 2a(18) of the Act does not authorize the allowance of costs "as between solicitor and lient," but is limited to "the costs fixede in the Act itself an dto the usual cost allowance fixede in other applicable statutes and by the rules of the Appellate Courts" (11174, p. 67).

That reasoning is not supported by the citation of any authority, and conflicts with the following historic facts:

(a) The Acts of 1800, 1841 and 1867 did not embody any express provision for the allowance of attorneys' fees of any character, but courts of bankruptcy nevertheless allowed them as equitable costs "as between solicitor and client," in a number of well-considered decisions,[13] which

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[13] (1868) *In re O'Hara*, D. C. Pa., Fed. Cas. No. 10465, 18 Fed. Cas. 622, 8 Am. Law Reg. (N. S.) 113; (1868) *In re Williams*, D. C. S. C., Fed. Cas. No. 17704, 29 Fed. Cas. 1324, 2 N. B. R. 83; (1869) *In re Jaffray*, D. C. Mass., Fed. Cas. No. 7170, 13 Fed. Cas. 284, 2 N. B. R. 452; (1869) *In re King*, D. C. Ind., Fed. Cas. No. 7780, 14 Fed. Cas.

practice was approved by this Court in *Trustees* v. *Greenough*, 105 U. S. 527,[14] and many of the subsequently enacted express provisions for allowances of attorneys' fees are largely declaratory of the practice so established and approved.

(b) In *Randolph* v. *Scruggs*, 190 U. S. 533, decided in 1904 under the Act of 1898, this Court followed the "equity precedents and practices" in a bankruptcy proceeding, and authorized the allowance, as equitable costs "as between solicitor and client," of attorneys' fees not expressly provided for by the Act.

(c) Under the Acts of 1841, 1867, 1898 and 1938, attorneys' fees not expressly provided for by the Acts have been allowed by courts of bankruptcy, as equitable costs

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503, 4 Biss. 319; (1869) *In re Schwab*, D. C. N. Y., Fed. Cas. No. 12498, 21 Fed. Cas. 763, 2 N. B. R. 488; (1869) *In re Mitteldorfer*, D. C. Va., Fed. Cas. No. 9675, 17 Fed. Cas. 537, 3 N. B. R. 1; (1869) *In re Montgomery*, D. C. N. Y., Fed. Cas. No. 9726, 17 Fed. Cas. 617, 3 N. B. R. 137; (1870) *In re New York M. S. Co.*, C. C. N. Y., Fed. Cas. No. 10208, 18 Fed. Cas. 155, 3 N. B. R. 627; (1871) *In re Comstock*, D. C. Mich., Fed. Cas. No. 3074, 6 Fed. Cas. 239, 5 N. B. R. 191; (1872) *In re Mansfield*, D. C. N. Y., Fed. Cas. No. 9048, 16 Fed. Cas. 659, 6 Ben. 284.

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[14] On Page 535, the Court quoted with approval the following statement by Judge Lowell: "* * * the practice under the Act of 1841 was to allow such a charge out of the assets, as I find by examining the records. My doubt was of my power in the premises under the fee bill of 26 February, 1853, 10 Stat. at L., 161, which does not appear to sanction it and does appear to be intended to cover the whole ground of taxation of costs at law and in equity and admiralty; and by the general orders, these petitions follow the rule of cases in equity in all matters of costs. Upon reflection I have concluded that the fee bill is, probably, intended to reach only taxable costs, commonly so called, and may have its full effect without being construed to take away the power of a court of equity to permit counsel fees to be taxed in those cases where a fund is in court upon or to which different parties have distinct rights or claims." The quotation is from *In re Jaffray*, D. C. Mass., Fed. Cas. No. 7170, 13 Fed. Cas. 284, 2 N. B. R. 452.

"as between solicitor and client," in many other clearly reasoned decisions.[15]

(d) The powers of courts of bankruptcy in municipal composition proceedings are "in addition to the jurisdiction otherwise exercised" by them. § 81. The "jurisdiction otherwise exercised" includes the power to "Tax costs and render judgments therefor" against "the successful party for cause," or "in part against each of the parties, * * * in proceedings under this Act." § 2a (18). They are also invested with such jurisdiction "in equity as will enable them to exercise original jurisdiction in proceedings under the Act." § 2a. The Act does not expressly limit the class or character of costs they may tax, nor prohibit the taxing of equitable costs "as between solicitor and client," and the cited authorities establish that they "are courts of equity and exercise all equitable powers unless prohibited by the Bankruptcy Act."[16]

(e) Prior to the 1938 Act, clause 18 in § 2 authorized courts of bankruptcy to "tax costs, whenever they are allowed by law, and render judgments therefor" against "the successful party for cause, or in part against each of the parties, * * * in proceedings in bankruptcy." By the 1938 Act, the phrase "whenever they are allowed by law," was stricken out as being meaningless, "because there is no law regulating costs in bankruptcy proceedings

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[15] Cases cited in footnote 13; also (1900) *In re Little River Lbr. Co.*, D. C. Ark., 101 F. 558; (1902) *In re Evans*, D. C. N. C., 117 F. 574; (1903) *Summers* v. *Abbott*, 8 Cir., 122 F. 36; (1903) *Beach* v. *Macon Grocery Co.*, 5 Cir., 125 F. 513; (1904) *Receivers* v. *Staake*, 4 Cir., 133 F. 717; (1905) *In re Lacov*, 2 Cir., 142 F. 960; (1941) *In re Keystone Realty Co.*, 3 Cir., 117 F. 2d 1003; (1942) *In re Swartz*, 7 Cir., 130 F. 2d 229.

[16] *Young* v. *Higbee Co.*, 324 U. S. 204.

and *bankruptcy courts should have the power to tax costs upon equitable principles.*''[17] And the words ''under this Act'' were substituted for the words ''in bankruptcy,'' so as to encompass the various new forms of proceedings, such as arrangements, corporate reorganizations, and the like, not authorized originally by the 1898 Act.[18] One new form of proceeding is a municipal composition. It was authorized by the Act of August 16, 1937, adding Chapter X to the 1898 Act, which Chapter became Chapter IX of the 1938 Act. As applied to both the old and new forms of proceedings, clause 18 and general order 34 ''are merely declaratory of the general powers of courts of equity, including courts of bankruptcy, over the allowance and apportionment of costs * * *.''[19]

Therefore, counsel submits that the declared purpose of the 1938 amendment was to eliminate any conflict between the statutory authority to tax costs ''whenever they are allowed by law,'' and the cited decisions that courts of bankruptcy are invested with jurisdiction to assess equitable costs ''as between solicitor and client.'' The purpose was to bring clause 18 in harmony with the cited decisions, by making it clear that courts of bankruptcy are invested with ''the power to tax costs upon equitable principles.'' The decision of the Court of Appeals, if allowed to remain in effect, will nullify that declared purpose in the Fifth Circuit, and may serve as precedent for nullifying it in other circuits.

Point IV

By misconceiving the ''true question'' presented, and denying the existence of the historic equity power of courts

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[17] Analysis of H. R. 12889, 74th Cong., 2d Sess. (1936) 13; House Report No. 1409 on H. R. 8046, 75th Cong., 1st Sess. (1937) 19—Emphasis supplied.

[18] 1 *Collier on Bankruptcy,* (14 Ed.) 285, § 2.70.

[19] 1 *Collier on Bankruptcy,* (14 Ed.) 287, § 2.71.

of bankruptcy to allow solicitors fees as equitable costs "as between solicitor and client," the Court of Appeals so far departed from the accepted and usual course of judicial proceedings as to call for the exercise by this Court of its power of supervision.

The Court of Appeals rested its decision on the narrow technicality that the end result of the successful appellate proceedings was the dismissal of the composition petition. It thought the allowance was sought "for defeating a municipal bankruptcy proceeding," and said the "true question" was whether or not the court of bankruptcy could and should award a fee to counsel for a creditor "who obtains the dismissal of the bankruptcy proceeding" (11174, p. 65). It reasoned that Chapter IX does not authorize fees "for opposing and wholly defeating" a plan of composition (11174, p. 66), and that allowances can be made only for services that "produce or aid in producing a plan" (11174, pp. 66-68).

That reasoning subordinates substance to form. It leads ultimately to this strange conclusion: If the reversal of the interlocutory decree had resulted in an amended plan increasing the amount or value of the consideration offered in retirement of the claims, Petitioners might have been entitled to an allowance for the benefits conferred; but because the grounds of reversal necessitated the dismissal of the proceeding, and made possible the enforcement and collection of the full former amounts of the claims, Petitioners cannot be compensated for the benefits they conferred.

The fact is that the Court of Appeals misconceived the "true question." Petitioners did not seek compensation for obtaining "the dismissal of the bankruptcy proceeding," nor for "opposing and wholly defeating" the so-called plan of composition. Instead, they sought it for successful appellate proceedings that added material value to the claims of the minority creditors as a class. That is the

underlying, substantial equity, as distinguished from matters of form and technicalities.

Petitioners did not merely protect and preserve existing rights, but rather gave back to the minority creditors that which they had lost. The interlocutory decree had scaled the claims proportionately, materially impaired their value, enjoined their enforcement, and constructively converted them into less valuable claims of smaller amounts. By the successful appellate proceedings, the decree was reversed and set aside, and the claims were restored not only to their former characters, but also to their former amounts. The restoration increased and added greatly to their value. Had the decree not been reversed, the minority creditors could never have received nor collected more than the reduced amounts of the claims, notwithstanding any supposed "adventitious improvement in the City's finances." The reversal of the decree was the sole and proximate cause of their being able to enforce the claims for the former full amounts.

The Court of Appeals also failed to apply the true reason why fees are dealt with "jealously." The reason is that by disallowing or holding fees to a minimum, larger dividends to creditors are made possible. But it also is true that to attain the same end, it is the policy of courts of bankruptcy to encourage and reward a champion who makes larger dividends possible by recovering property or a fund for the benefit of creditors, or by protecting their rights and claims from spoilation at the hands of an oppressor. §64a(1) and (3).

As pointed out in several cases cited,[20] one creditor may

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[20] *In re O'Hara*, D. C. Pa., Fed. Cas. No. 10465, 18 Fed. Cas. 622, 8 Am. Law Reg. (N. S.) 113, *In re Williams*, D. C. S. C., Fed. Cas. No. 17704, 29 Fed. Cas. 1324, 2 N. B. R. 83; *In re Jaffray*, D. C. Mass., Fed. Cas. No. 7170, 13 Fed. Cas. 284, 2 N. B. R. 452; *In re Little River Lbr. Co.*, D. C. Ark., 101 F. 558.

not have sufficient economic interest to justify the expense of defending the rights of his class against unjust or oppressive schemes or practices, if he must bear the entire expense, as in most cases he would lose even though he won. In the instant case, had not Petitioner's clients championed the rights of the minority creditors by obtaining the reversal and setting aside of the interlocutory decree, their claims would have continued to be worth only approximately fifty cents on the dollar, instead of their full amounts. The minority creditors would have been "bludgeoned into submission" had the interlocutory decree remained in effect. Absent success in the appellate proceedings, the non-appealing creditors could never have been put to one cent of expense, and could never have collected more than approximately fifty cents on the dollar. They are now asked to pay only their fair share of the burden *from their gains.*

Counsel urges that the misconception of the "true question," and the resulting denial of the existence of an historic equity power of courts of bankruptcy, call for the exercise by this Court of its power of supervision.

Point V

The holding of the Court of Appeals that when equitable costs "as between solicitor and client" are allowable, they should be sought "in the name of the party," and it is not permissible for the affected attorneys to petition for the allowance directly to themselves, is in direct conflict with controlling principles enunciated by this Court in *Central R. & B. Co.* v. *Pettus,* 113 U. S. 116.

All that need be said in support of this point is, first, the holding of the Court of Appeals is not buttressed with the citation of any authority, and, second, this Court has decided: "And when an allowance to the complainant is

proper on account of solicitors' fees, it may be made directly to the solicitors themselves, without any application by their immediate client." *Central R. & B. Co.* v. *Pettus, supra.*

Respectfully submitted,

MILLER WALTON,
On his own behalf and as
Attorney for his co-petitioner.